Embedded *Finance*

Opportunities for ERP and payroll SaaS providers

OC&C Strategy consultants

uncommon sense™

EMBEDDED FINANCE IS A MATERIAL OPPORTUNITY FOR SAAS ERP AND PAYROLL PROVIDERS. OC&C'S RESEARCH SUGGESTS THAT AN **EBITDA UPLIFT OF 20-30% COULD BE ACCESSIBLE ON A 2-3 YEAR TIMESCALE**, WITH A MUCH LARGER OPPORTUNITY AVAILABLE IN THE LONGER TERM.

We believe that a new generation of specialist embedded finance providers can offer **rapid time-to-value** and a proposition that allows you to keep **full control** of the customer relationship and workflow.

We'd encourage you to take this opportunity seriously.

In this paper, we aim to provide a short briefing on the opportunity. We will outline:

1. **How the Embedded Finance value chain works in ERP and Payroll** – and in particular how it now enables ERP and payroll software players to offer valuable financial services to customers with very low friction and no regulatory exposure.

2. An overview of **embedded finance products with most traction** today.

3. A **worked example showing how a 20-30% EBITDA uplift is available** on a 2-3 year time frame and an illustrative view of **how transformational EBITDA uplift might be achievable** over time – something that has already been achieved by some vertical software players (e.g. Toast in US Hospitality).

4. **Your potential options to move ahead** and capture the opportunity.

The Embedded *Finance* value chain

THE VALUE CHAIN FOR EMBEDDED FINANCE IS TYPICALLY COMPOSED OF THREE STEPS, FROM THE END CUSTOMER (SUCH AS AN SME) TO A FULLY 'REGULATED' FINANCIAL ENTITY, TYPICALLY VIA A SOFTWARE PLATFORM (E.G. ERP SOFTWARE) AND A FINANCIAL SERVICES ENABLER.

We note that more financial services enablers are moving towards getting full banking licenses (e.g. Swan.io in France) and banks are launching own Banking as a Service (BaaS) platforms to provide embedded finance experiences (e.g. NatWest bank launching Boxed).

The implication for SaaS providers is that provision of financial products is becoming increasingly straightforward and does not require building in-house fintech capabilities.

EXHIBIT 1: EMBEDDED FINANCE VALUE CHAIN IN B2B SAAS

End User / Customer	→	Software Platform	→	Financial Services Enabler
SMEs Users of SaaS application e.g. ERP and potential buyers of financial products. **Fragmented** e.g. shops, restaurants		**B2B SaaS Vendors** Cloud-enabled SaaS provider and owner of customer relationship and customer journey. We are focusing on ERP and payroll software providers in this paper. VISMA sage xero		**Mix of Regulated and Unregulated Entities** Varied eco-system of providers enabling the integration of financial products into non-financial customer workflows. Mix of regulated and unregulated entities, with the former able to issue financial products directly (e.g. via own banking license). Includes multiple activities such as onboarding of customers, compliance services, provision of technology layer and issuing of licensed financial products. **Embeddable Solutions** ⟷ **API-enabled Banking** weavr swan solarisBank NatWest toqio Modulr Clear.Bank

Emerging Embedded *Finance products*

FINANCIAL PRODUCTS CAN BE EMBEDDED THROUGHOUT ERP AND PAYROLL SOFTWARE WORKFLOWS.

ERP: we see several touchpoints for embedded finance in the typical ERP software workflow, starting from the automation of domestic and international payments for accounts payable and accounts receivable (e.g. via a 'Pay Now' button), the issuing of company cards to track and monitor expenses (e.g. for international travel) and providing access to financing opportunities via loans (e.g. pre-approved business loans) and invoice factoring.

Payroll: the typical payroll software workflow also presents several opportunities for embedded finance, particularly around the processing of international payments (e.g. via localised bank accounts or facilitated international transfers), earned wage access, payment of temporary and hourly workers and management of employees perks and benefits (e.g. via prepaid cards).

EXHIBIT 2: EMBEDDED FINANCE IN ERP AND PAYROLL WORKFLOWS

ERP Software Workflows

Payments Processing & Monitoring
- Accounts payable automation
- Accounts receivable automation (e.g. 'Pay Now' button)
- Subscription payments
- International transfers / payments

Financing
- Business loans
- Invoice factoring
- Working capital loans

Expense Tracking
- Company expenses cards (e.g. for travel)
- Online marketing spend (via ad-hoc cards)

Payroll Software Workflows

Workforce Management
- Payroll payments automation
- Earned wage access
- Paying unbanked / temporary / seasonal workers
- Localised bank accounts
- International transfers / payments

Employee Benefits & Rewards
- Employee perks (e.g. via pre-paid cards)
- Automated reward schemes

Our research suggests 'cost to play' is c.30% of incremental revenue generated through embedded finance products.

Whilst there are likely many other financial products with the potential to be embedded into software workflows (e.g. business insurance), we decided to focus on **company cards, business loans** and **international transfers automation** for our modelling. These products are currently seeing more traction, with multiple examples of successful deployments.

The typical set-up and economics for the products listed above are as follow:

- **Company Cards:** typically three sources of revenue which are shared by the members of the value chain (SaaS vendor, financial service enabler, financial institutions):
  - Monthly flat fee per card user (e.g. £10 / month)
  - Revenue generated on interchange rate (which is not capped in UK and EEA for business cards)
  - Interest generated on funds deposited on the card (for debit cards only)
- **Business Loans:** revenue share on the interest fee charged to the end user – which is then shared between the BaaS provider and the SaaS vendor
- **International Transfers:** revenue per transaction, with margin shared by the members of the value chain (SaaS vendor, financial service enabler and international payment enablers e.g. Mastercard)

Cost to play: The costs to a SaaS provider to offer embedded financial products mainly revolve around three areas:

- Recurring fee paid to financial services enabler – typically in the £1000-3000 range / year
- Technical integration – upfront development costs during launch phase to 'embed' the financial products in the user experience (but limited ongoing development after)
- Customer service / training – to provide first line support to end customers who purchase financial products (e.g. if a card payment is declined)

Our research suggests 'cost to play' is c.30% of incremental revenue generated through embedded finance products. These costs are mostly fixed or semi-fixed and therefore likely to benefit from scale, as the customer attachment rate increases.

Estimating EBITDA uplift for selected Embedded *Finance Products*

WE BELIEVE THE SIZE OF THE OPPORTUNITY TO BE MATERIAL, **POTENTIALLY LEADING TO A 20-30% EBITDA** UPLIFT FOR AN EMBEDDED FINANCE PROPOSITION DEPLOYED AT SCALE.

Below is an illustration of the potential EBITDA impact on a hypothetical scale B2B SaaS company, with some conservative assumptions on revenue share distribution, attachment rate and cost to play. We used an illustrative B2B SaaS provider with assumed revenue of £100m, 30-40% EBITDA margin and Average Spend / Customer of £2000 / Year.

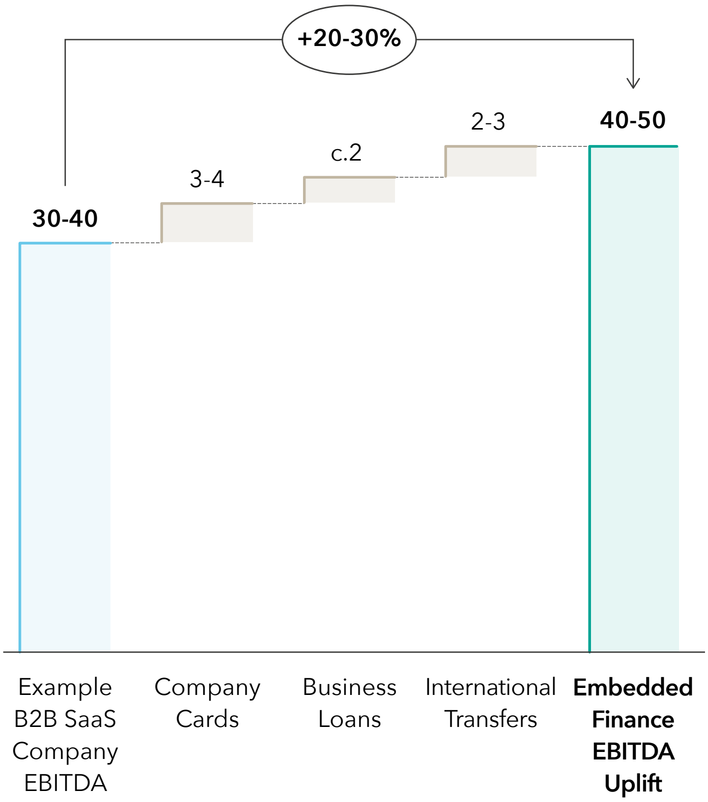
Our calculations suggest a potential **20-30% EBITDA uplift** for an embedded finance proposition deployed at scale – taking average annual spend values for UK SMEs on Company Cards, Business Loans, and International Transfers, with conservative assumptions on revenue share, attachment rate and cost to operate.

Our estimate is likely conservative as it does not include benefits from other factors such as increased customer retention from providing more mission critical services (e.g. financing).

It is possible to obtain a significantly larger EBITDA uplift with a larger number of embedded financial products, a higher attachment rate among end customers or a higher revenue share for the B2B SaaS provider. The sensitivity table below shows EBITDA uplift with varying belief conditions on revenue share distribution and attachment rate. An EBITDA uplift of 50-55% is possible with 70% revenue share in favour of the SaaS provider and a customer attachment rate of c.15%.

EXHIBIT 3: EBITDA IMPACT ILLUSTRATION – BASE CASE

EBITDA Opportunity by Embedded Finance Product, (£m)



Key Assumptions for Illustrative B2B SaaS Provider

	Company Cards	Business Loans	Int'l Transfers
Revenue (£)	£100m		
EBITDA %	30-40%		
# of Customers	50k		
Average Spend / Size	£6k / card / year	£25k	£75k
Average Interchange Rate / Interest / Fee	1-2%	4-6%	1-3%
Revenue Share for SaaS Provider	50%	50%	50%
Attachment Rate	10%	10%	10%
Cost to Play (% of Revenue Share)	30%	30%	30%

Source: Expert Interviews, CapIQ, OC&C analysis.

Our estimate is likely conservative as it does not include benefits from other factors such as increased customer retention from providing more mission critical services.

EXHIBIT 4: EBITDA IMPACT ILLUSTRATION – SENSITIVITY TABLE

		Revenue Share for SaaS Provider				
		30%	40%	50%	60%	70%
Customer Attachment Rate	5%	7%	9%	12%	14%	16%
	10%	14%	19%	23%	28%	33%
	15%	21%	28%	35%	42%	49%
	20%	28%	37%	47%	56%	66%
	25%	35%	47%	59%	70%	82%
	30%	42%	56%	70%	84%	98%

OC&C Base Case

There are examples of SaaS businesses (mainly in vertical software) achieving material incremental revenue and profit through financial products. For instance, Toast – a US provider of PoS software and systems for restaurants – generated c.80% of FY22 revenue and gross profit through finance technology solutions, including payments processing and business loans.

In addition to bottom line impact, we believe there are other reasons for which ERP and payroll providers should be interested in embedded finance (though these have not been explored in detail for the purpose of this paper):

1. **Increased customer retention** – as 'enabling' the delivery of financing and banking services widens the set of mission critical services offered by SaaS providers.

2. **Potential to add value to value chain participants with proprietary data** – as ERP and payroll providers have often access to unique insights about their customers which could be used to create tailored financial products.

3. **Ability to capture even more data** – as typical embedded finance customers journeys remain 'captive' within the SaaS application.

Accessing the Embedded *Finance opportunity*

IT IS POSSIBLE TO GET GOING RAPIDLY TO TACKLE THIS OPPORTUNITY, **WITH PARTNERSHIPS PRESENTING AN ATTRACTIVE ALTERNATIVE** TO BUILDING CAPABILITIES IN-HOUSE.

We note several scale B2B SaaS providers are taking action and building embedded finance capabilities organically and inorganically:

- Xero, the Australia-based accounting software provider, enables customer to embed a 'Pay Now' button in their invoices which is linked to international payment providers (e.g. Stripe) and supports mobile payments (e.g. Apple Pay).
- CloudPay, a rapidly growing international payroll provider, is enabling temporary and hourly workers to access their earned wage earlier through its 'NOW' service; access to CloudPay NOW is also offered as an employee perk in partnership with Perkbox.
- International HCM & payroll provider IRIS Software Group is partnering with fintech provider UNIPaaS to offer embedded B2B payments to its customers.

Partnerships with Financial Services Enablers present an attractive alternative for scale B2B SaaS providers to get going rapidly, with a few important advantages including:

- No need to acquire / build a business with a fundamentally different business model (e.g. a lending provider).
- No balance sheet risk.
- No need to build 'pipes' into banks and other financial institutions.
- Regulatory hurdle taken care of (e.g. banking license).

For instance, Xero cited 'differences in business model' as one of the reasons for selling lending platform Waddle to Commonwealth Bank of Australia in 2023.

However, several potential 'endgames' are available, each likely to require a tailored strategic approach. For example, a major ERP software provider for SMEs could aim to provide fully embedded banking to its customers together with a 'regulated' entity / bank – Sage and Tide appear to be moving in this direction with their partnership.

If partnering with an external provider is the preferred approach, then multiple options are available across the UK and EEA. The competitive landscape for BaaS / embedded finance providers is still relatively fragmented, and rapidly evolving.

We see players distinguishing along two main dimensions:

1. Build-your-own solution vs ready-made solutions.
2. Customer ownership – with customer owned by either the SaaS provider or the financial institution (with SaaS platform providing referrals).

We note players exist in each of the resulting 'boxes', with the picture below showing examples of players active in UK and EEA.

EXHIBIT 5: EMBEDDED FINANCE LANDSCAPE IN UK & EEA

	Build-Your-Own Financial Solution	Ready Made Financial Solutions
SaaS platform owns the customer *Journey is fully embedded in SaaS workflow*	**Banking-as-a-Service** swan Modulr solarisBank	**Fully Embeddable Financial Solutions** weavr toqio
Partner owns the customer (e.g. BaaP) *SaaS partner provides referrals*	**Banking-as-a-Platform** stripe Starling Bank BOXED	**API-enabled Standalone Finance Solutions** stripe CONNECT bill.com

CASE STUDY

WEAVR IS ONE OF FEW PLAYERS PROVIDING READY-MADE EMBEDDED FINANCE SOLUTIONS LICENSED FOR BOTH THE UK AND THE EEA.

OC&C's friends at Weavr provide white-label ready-made embedded finance products for SaaS providers to integrate into their ERP or Payroll interfaces. The business primarily partners with horizontal and vertical software providers, with 100+ current SaaS customers.

Weavr's proposition is centred around 'Financial Plug-ins' designed for specific embedded finance use cases such as Accounts Payable, Expense Management, Employee Benefits and Earned Wage Access. Key characteristics include:

- Operates with financial partners licensed in the UK and in the EEA.
- Required banking capabilities are included with each Plug-in, preventing the need for additional contracts between the SaaS provider and financial institutions.
- Bundled compliance services, pre-empting the need for specialist compliance technology (e.g. data security, financial crime).
- Availability of non-financial add-ons tools to enhance 'Financial Plug-ins' including go-live activation, customer support tools and data insights.

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OC&C can help you navigate key strategic questions on this topic

At OC&C, we are passionate about the rapidly evolving world of B2B SaaS – having worked with many of the leading players in Europe. We love helping our clients to be at the forefront of commercial opportunities enabled by disruptive technological change.

There are multiple ways in which we could support you at different stages of your journey with embedded finance, including:

- Determining a structured process for experimentation, evaluation and prioritisation of the opportunity
- Building on your initial success to think about scaling: defining an ambitious or transformational plan
- Assessing potential partners or M&A targets

Please get in touch to share your experience or continue the discussion:

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